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SUBJECT: ESTONIA: SCENESETTER FOR DEPUTY SECRETARY OF  
ENERGY SELL DELEGATION

¶1. (SBU) Summary: The last year has been a banner period for U.S.-Estonian bilateral relations, including President Bush's November visit to Tallinn, Foreign Minister Paet's visit to Washington for a celebration of the 85th anniversary of diplomatic relations, and President Ilves' June visit to Washington. Estonians are very grateful for U.S. support in the aftermath of their government's decision to relocate a Soviet war memorial known as the "Bronze Soldier" in late April. In regards to the formerly contentious issue of membership in the Visa Waiver Program, Estonia's recent progress and U.S. Congressional action put the country on track to join the program possibly as soon as next year.

¶2. (SBU) Three and a half years after NATO and EU accession, Estonia remains a strong ally on all fronts. It is deeply committed to trans-Atlantic security institutions and pro-free market economic policy. Estonia is a steadfast ally in the Global War on Terror (GWOT) in both Afghanistan and Iraq, and an effective role model for democracy in the former Soviet states and beyond. Estonia is gradually becoming a more vocal member of the EU and is a strong supporter of both EU and NATO enlargement. The Estonian economy continues to boom, although inflation and the current account deficit remain high while the labor market is increasingly tight. Relations with Russia remain difficult, particularly after the move of the "Bronze Soldier" monument. Following cyber attacks on Estonia's high-tech infrastructure in May, the GOE raised the national security implications of the issue at NATO, within the EU and bilaterally with its allies. End summary.

¶3. (SBU) This has been a big year for U.S.-Estonian bilateral relations. President Bush came to Tallinn last November, the first ever visit to Estonia by a sitting U.S. President. In June, Estonian President Toomas Hendrik Ilves met with President Bush at the White House. Following riots, cyber attacks and deteriorating relations with Russia in late April and early May, the United States voiced strong public support for Estonia. (Note: The United States strongly supported the Estonian government's right to decide what to do with the "Bronze Soldier" and decried Russia's failure to provide adequate security for the Estonian embassy in Moscow. At the same time, we called for dialogue, both between Estonia and Russia and between ethnic Estonian and Russian residents of Estonia as the best way to resolve difficult issues and build mutual understanding. End Note.) In addition, the three Baltic Foreign Ministers recently met with Secretary Rice to mark 85 years of relations with the United States. Appreciation for U.S. non-recognition of the Soviet occupation of Estonia remains an important source of good will towards the United States. However, one major challenge for our public diplomacy efforts is to engage the next generation of Estonians to ensure that American-Estonian relations will remain strong for the long term.

## FOREIGN POLICY AND SECURITY

¶4. (U) GLOBAL WAR ON TERROR. Estonia is a strong supporter of the U.S. position in the GWOT. Estonian troops participate in NATO operations (in Afghanistan, Kosovo, and Iraq), EU operations (the EU's Nordic Battle Group), Operation Enduring Freedom in Iraq, and other missions (including the UN mission in Lebanon). In Afghanistan, Estonian troops serve as part of a UK-led Provisional Reconstruction Team in Helmand Province, the epicenter of Afghanistan's poppy producing region. In Iraq, Estonian soldiers are embedded with U.S. troops in some of the toughest counter-insurgency operations outside of Baghdad. On June 23, 2 Estonian soldiers were killed in Afghanistan. In 2004, 2 others were killed in Iraq. Overall, 8.2% of Estonia's military is currently deployed overseas, while the country is on track to meet its NATO commitment of devoting 2% of its GDP to defense spending (currently at 1.83%). Estonia is a vocal supporter of NATO enlargement; GOE officials often speak out on the importance of bringing Balkan and Eastern European countries into NATO in order to cement democratic and free-market reforms there.

¶5. (U) REGIONAL DEMOCRACY PROMOTION. Estonia plays an active role in encouraging democratic reforms and economic development in several former Soviet states. Estonia's experience of transforming itself from a Soviet-occupied country into a healthy democracy with a booming economy has given it immense credibility in the region in promoting democracy and transformational diplomacy. The GOE has provided training in law enforcement, judicial reform, freedom of the press, democracy building, economic and market reforms, and IT to civil servants from the Balkans, Georgia, Moldova, and the Ukraine. Georgia is of

particular importance for the GOE -- Estonian President Ilves, Prime Minister Ansip, and Foreign Minister Urmas Paet have all visited Tbilisi to strengthen ties between the two countries. Former Prime Minister Mart Laar serves as a personal advisor to Georgian President Mikheil Saakashvili on political and economic reform.

## ECONOMIC PERFORMANCE

¶6. (U) Estonia's economy is probably the most dynamic of the "Baltic Tigers," and has been growing at 7-11% per year for the past seven years. The state budget has been in surplus since 2001, (currently 3.3% of GDP) and unemployment is currently 5.3% and falling. The biggest challenges facing the economy are: a labor shortage, a growing current account deficit, and inflation (caused primarily by rapid growth, rising energy costs and rising wages). The national currency, the Kroon, is pegged to the Euro. Estonia hopes to join the Euro zone by 2011. (Note: Estonia meets all Euro criteria except for inflation. End Note.)

¶7. (SBU) Since the early 1990s, consecutive Estonian governments have backed a business- and investor-friendly economic policy featuring a flat 22% tax on personal income and no tax on reinvested profits. Leading sectors include computer, software and cellular technologies, tourism and manufacturing. The United States is the eighth largest foreign direct investor, but U.S. direct investment accounts for less than 2.5% of total FDI, well behind the Swedes and Finns, who together account for more than 80% of the total. Estonia is best known for its highly developed IT sector and widespread use of technology in government and daily life. Internet usage in Estonia is over 60%, and online banking is upwards of 80% -- both the highest in Europe. Cabinet ministers work on the basis of e-government and Estonia was the first country in the world to offer e-voting in a nationwide election. The development and support offices of the internet-telephone giant Skype -- now owned by E-Bay -- are located here.

¶8. (U) Another central issue to the Estonian economy is energy security. Large domestic oil shale reserves allow Estonia to remain relatively independent of Russian energy supplies. The proposed NordStream gas pipeline from Russia to Germany may pass through Estonia's economic zone in the Baltic Sea, very close to its territorial waters. GOE officials state firmly that Estonia will closely study the environmental and security issues related to the project. Speaking at the Center for Strategic and International Studies (CSIS) in late June, President Ilves said that Germany's "failure" to consult with other EU members regarding NordStream undermined trust and highlighted the need for a common EU approach to energy security.

#### RUSSIA

¶9. (SBU) RUSSIAN RELATIONS. Estonia's relationship with Russia is difficult and complicated following nearly 50 years of Soviet occupation. While the countries share trade and investment ties, they have not been able to conclude a border treaty. Depending on the political climate, trucks crossing from Estonia into Russia may encounter delays of up to several days. Estonia's decision to relocate the "Bronze Soldier" prompted riots by ethnic Russians in Tallinn. Following the riots, Russia put heavy economic and diplomatic pressure on Estonia - including refusing to disperse a mob outside the Estonian Embassy in Moscow for several days, limiting rail and truck traffic across the border and encouraging a boycott of Estonian goods. At the worst point, rail traffic (oil, coal, wood and other materials) was down by 50% - significantly reducing Estonia's transit revenues and complicating supply lines for Estonian companies. Rail traffic has still not returned to normal levels.

¶10. (SBU) Ethnic Russians make up approximately 25 percent of the population of Estonia. Russia has frequently complained about GOE treatment of its Russian speaking minority. However, until the Bronze Soldier riots, Estonia's efforts to integrate its minority population were viewed as a model for the region. While Estonia can still point to significant accomplishments of its integration strategy, the riots revealed deep fissures remain between ethnic Russians and Estonians living in Estonia. The GOE, which has traditionally engaged in language-based integration programs, is working on a new strategy that will continue with language programs, but also focus on society building and cultural understanding among Estonians of all ethnicities.

#### VISA WAIVER

¶11. (SBU) Securing visa-free travel to the United States for Estonian citizens remains a priority for both the GOE and Estonian public. Senior GOE officials regularly raise the issue of membership in the U.S. Visa Waiver Program (VWP) at all levels with the USG. Estonia's recent progress toward meeting the VWP criteria, and U.S. Congressional action, put the country on track to join possibly as soon as 2008.

#### PHILLIPS